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THE COST TO OCCUPY HOUSING



SANTA CLARA COUNTY



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THE COST TO OCCUPY HOUSING



SANTA CLARA COUNTY

The Joint Cities-County Housing Element Program:

CITIES:

Campbell
Cupertino
Gilroy
Los Altos
Los Altos Hills
Los Gatos
Milpitas
Monte Sereno
Morgan Hill
Mountain View
Palo Alto
San Jose
Santa Clara
Saratoga
Sunnyvale

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*Summer 1970

THE COST TO OCCUPY HOUSING

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SUMMARY

Housing costs are rising dramatically in Santa Clara County. This has been coupled with an increasing emphasis on construction of higher priced units. The result is a critical shortage of houses and rental accommodations available to low and moderate income households in the County. Inflationary pressures and the diminution of money for mortgages have increased the initial and monthly costs to occupy housing. Proposals for action can be meaningfully offered only after the problem is understood. This study provides background data on the high costs of housing. Attention is directed on four areas of study.

INITIAL OCCUPANCY COSTS

Two models are developed for the analysis of entry costs in a single family house. For a conventionally financed \$20,000 home, the initial cost to occupy is about \$5,500. For the same house financed under FHA insurance, the cost is about \$2,300. Two rental unit models are also developed using countywide medians. For a two-bedroom unfurnished apartment the initial cost to occupy is \$360, and a three-bedroom unit costs \$405. Incidental costs, not directly related to rental fees or mortgage financing, amounted to \$57 for an apartment and \$73 for a house.

MONTHLY OCCUPANCY COSTS

Monthly housing costs include debt service, taxes, insurance, maintenance and repair, and heating and utilities. For an FHA-insured house of \$25,000 value, monthly occupancy costs are about \$247 a month. For a conventionally-financed house of the same value, monthly costs are \$260 a month. Rental apartments of two and three bedrooms have monthly costs of \$178 and \$202 respectively.

PROGRAMS AND POLICIES TO REDUCE HIGH OCCUPANCY COSTS

Federal programs for low cost housing have been implemented on a limited scale in Santa Clara County. Recently there has been a surge of interest in non-profit sponsorship of low and moderate income housing as socially-motivated groups seek to provide decent housing for low income families. The housing problem is being attacked on a regional basis as witnessed by the efforts of the Joint Cities-County Housing Element Program.

Local efforts to obtain low cost housing face the problem of inadequate financing. However, not all problems are of a fiscal nature. Other cities and states have taken a leading role in passing enabling legislation to allow new and innovative techniques to be used in attacking the problem of providing decent housing for low income families.

PROPOSALS

Summary of Proposals for Reducing the Cost to Occupy Housing.

1. Property Tax Abatement. Property taxes have an especially onerous impact upon low-income families. The state should offer partial tax abatement by reimbursing that portion of residential property tax above a specified percentage of the family income. Renters would also benefit if 25 percent of annual rents is treated as property tax.
2. Reducing Down Payments. Down payment requirements are one of the greatest obstacles to home ownership by low and moderate income households. The state should make loans, for the amount of the down payment, which would become due after the first mortgage was paid off.
3. Lease and Sale of VA and FHA Foreclosed Dwellings. The Housing Authority should acquire foreclosed dwellings for its leased housing program and for ownership. Recent federal proposals offer the opportunity for home ownership by low and moderate income households by counting a portion of the subsidy and rental as equity for future purchase.

4. Cost Limit Aid. The state should make interest-free loans to developers of low cost housing so they may fall within federal cost limitations.
5. Replacement Housing as a Cost of Public Improvement. The cost of replacement housing should be considered as a direct cost of public improvement. At the state level, the Ralph Act has provisions for the replacement of housing removed for state highway construction. Such provisions should be extended to other public actions by all levels of government.
6. Certificate of Decent Housing. Substandard housing should not be subsidized. Yet housing subsidies do not require recipients to occupy standard quality housing. Landlords should be required to have a Certificate of Decent Housing, issued by a housing inspector, before they rent a unit to welfare recipients.
7. Conditional Income Supplement. A greater choice of housing consumption can be given to low income families through the issuance of a conditional income supplement. Cash grants of prescribed amounts would be allocated with the stipulation that the recipient occupy standard quality housing. Any unspent portion accrues to the family thus providing an incentive to shop around.
8. Landlord-Tenant Adjudication Committee. A quasi-judicial committee whose arbitration would be binding, could resolve many landlord-tenant issues without recourse to the courts.
9. Accelerated Depreciation on Rehabilitated Property. Rehabilitation of older property often results in increased rents for the tenants. In order to keep costs down so that low and moderate income families would not be forced to relocate, rehabilitated property should be allowed accelerated depreciation at the same rate as for new construction.

10. Write-Down Subsidies. Property acquired and resold by a local renewal agency for rehabilitation purposes has a deflated market value. The differential between the acquisition cost and the market value should be given to an owner if he agrees to rehabilitate his unit. This would mitigate the necessity to relocate households displaced by the urban renewal process. This program should be extended outside urban renewal areas and code enforcement made uniform.

Summary of Proposals to Increase the Supply of Mortgage Funds.

1. State Below Market Loans. Federal housing programs lack adequate funding. A state program to augment federally reduced interest programs could increase the supply of housing and allow greater flexibility to meet local conditions.
2. Use of Short-Term County Funds. The County should deposit part of its short-term funds in banks and savings and loan companies that agree to make funds available for interim financing on low and moderate income housing.
3. State Mortgage Authority. The state could create a secondary market for older, lower-yield mortgages. The money which is thus freed could be tied so that 25 percent of the total would go for low and moderate income housing at below market rates.
4. Differential Reserve Requirements on Loans. The supply of funds for low and moderate income housing can be increased by placing a reserve requirement on loans rather than deposits.
5. Direct Federal Lending. The interest paid on long term mortgages can amount to more than the principal. Direct federal lending may be cheaper if budgetary constraints are removed to enable capital purchase of housing rather than subsidizing market interest rates.

6. Federal Insurance for Conventional Mortgages. Federal insurance programs have brought the possibility of home ownership within the reach of many families. The benefits of mortgage insurance should be extended to conventionally financed loans.
7. Pension Fund Investment. In order to maintain their tax free status, pension and retirement funds should be required to invest a greater portion of their assets in home mortgages.
8. Mortgage Insurance for Rehabilitation. Older areas of the cities and County are in special need of money for rehabilitation and maintenance. Past policy has been to "red line" such areas and mortgage insurance was not granted in the circumscribed area. Local government should initiate an insurance program to augment federal programs in order to prevent further blight and to maintain the present stock.
9. Variable Interest Rates. The flow of money going into home mortgages diminishes in periods of tight money and rising interest rates because the mortgage is not an attractive investment when compared to short term government notes or commercial paper. To make the mortgage more competitive, a variable interest rate should be initiated. Interest rate would not be fixed for the duration of the amortization period but would fluctuate, by some formula, with the current rate of return on some high grade industrial paper.
10. Split Mortgages. There is no reason why the home site should be purchased and amortized along with the building shell and improvements. By doing so, the buyer is forced to build an equity--which he may not want or cannot afford. A split mortgage, which would amortize the building shell in 50 years,

improvements such as appliances and heating in 10 years, and not amortize the property at all, could bring down the cost of home ownership and allow low and moderate income households to experience home ownership.

11. Piece of the Action Mortgages. Mortgage lenders have sought to increase the yield on their investment through such innovations as points and discounts. Yet in periods of tight money, they are not sufficient to assure an adequate supply of funds for home mortgages. The piece of the action mortgage allows the lender to share in a portion of the profits of rents besides his interest for use of the money. This type of inducement could draw more funds into the mortgage market.
12. Industry Seed Money. Industry should share the cost of relieving the housing shortage. A local tax, based on the number of anticipated new jobs to be created, should be assessed on local employers. The funds could be used to provide "seed money" for non-profit sponsors of low and moderate income housing.

PREFACE

Considerable concern has been expressed by two national commissions charged with examining this nation's housing and urban problems as to the ability of low and moderate-income families to obtain a decent home. The price of a decent home in a suitable living environment varies with the size, age, location and type of tenure of the dwelling unit. To better appreciate the plight of low and moderate-income families in their attempt to obtain a decent home, some background information on the housing situation in Santa Clara County may be useful.

In 1966, 32 percent of the new tract homes occupied in Santa Clara County were priced under \$20,000. During 1969, only 5 percent of the homes occupied were in this price range. Occupancies in homes over \$30,000 had increased from 20 percent to 35 percent during the same period. Rents on apartment houses further reflect the current low vacancy rates and tight money in the home mortgage market. A San Jose State College study conducted in 1967 revealed that over 60 percent of the apartment house owners had raised their rents during the previous six months. A similar study conducted in March of 1969 also revealed that over half of the owners had raised their rents in the previous six months. Rents have been climbing steadily since 1967 so that by March of 1969 only 3 percent of the two-bedroom apartments in the County rented for less than \$120 a month.

These factors have contributed to a critical shortage of houses and rental accommodations available to low and moderate-income households in the County. In 1966 almost 40,000 households in Santa Clara County had incomes of less than \$4,000 a year. It is estimated that in 1969 there were still approximately 39,000 households in this category. Using the rule of thumb that a family can afford a home equal to twice its annual income, or monthly rental equal

to 25% of its monthly income, it appears that a substantial number of households are priced out of the new house and rental market.

A number of factors contribute to the difficulty low and moderate income families face in trying to obtain decent housing. Included are factors of discrimination, lack of information, inadequate income, inability to meet required down payments, rapidly rising prices of new and rental housing, and limitations placed on local housing authorities.

In his report "The Crisis We Face: Housing for Low Income Families in San Jose" Congressman Don Edwards expressed the concern that "housing is San Jose's most vicious social ill, hurting the poor and the minorities, our most defenseless citizens." A 1969 study of the Gardner district of San Jose by Stanford University reported on the extremely low expectations of many people living in areas of poor housing. The report further stated that "the same sense of resignation was noted when interviewees were questioned about other things which affect their daily lives, such as transportation, recreation, neighborhood hygiene and esthetics, shopping centers, noise, health care, etc." Others have suggested that high costs may prohibit the marginal person from making a move to better housing, inhibiting geographic and social mobility. It has also been hypothesized that poor housing is related to poor mental and physical health, poor educational performance by children, social deviance, increased dependence on welfare, geographic concentration of racial and ethnic minorities, and unemployment. It remains open whether the cycle of poor housing, poor health, inadequate education and low paying jobs can be directly attributed to high housing costs. However, one point is clear. Given a certain amount of money, the more a family is forced to spend for housing, the less it has to spend on food, education, clothing, and other essentials.

This study examines the initial and monthly costs to occupy rental and owner-occupied single-family housing. There are basically three types of housing expenditure decisions--the decision to purchase, rent, or rehabilitate an existing structure. Each of these decisions involve different levels of costs with the decision to purchase usually requiring the greatest initial cash outlay. The particular type of housing which a person occupies is an economic function of his liquidity position and his ability to qualify for a mortgage loan. Liquidity refers to the cash or near cash assets which a person possesses. These funds are used either to meet down payment and closing costs or to serve as a reserve on which to secure a loan on more favorable terms. The ability to qualify for a loan is determined to a large degree by the income level of the potential mortgagee. By identifying and giving a range of values to the various costs involved in occupying a home, we can better understand the dilemma faced by low and moderate-income families in their attempt to occupy a decent home.

Information on practices and policies of the various institutions involved in the housing process was obtained through a review of secondary sources, supplemented by interviews with persons dealing with the housing process in late 1969, early 1970. Data from these sources formed the basis for development of models which represent typical values for the various components of initial and monthly occupancy costs. A perusal of available data indicates that the single-family dwelling and rental apartments constitute the majority of housing units available for occupancy. Mobile homes are not considered in this study.

After entry and monthly occupancy costs are identified and given quantitative dimensions, local programs and policies to facilitate these costs are analyzed. Other programs not locally available are then examined, and finally, proposals to ease the burden of high occupancy costs and to increase the supply of funds for low and moderately priced housing are presented.

CHAPTER I INITIAL OCCUPANCY COSTS

INTRODUCTION

A number of costs are incurred incident to occupying a dwelling unit. They include down payment and prepaid interest on the mortgage loan, title search and insurance, lender's service fee, transfer taxes, and rental and other deposit fees. The exact amount of initial occupancy costs varies widely from place to place. In Santa Clara County, the average entry cost for a new FHA-insured home in 1968 was approximately \$2,500. For rental units, entry costs vary considerably, as there are no consistent policies on deposits for cleaning or rent security.

One of the major problems faced by low and moderate-income families seeking decent housing is their inability to meet the initial costs. This problem is related to an insufficient income to allow for an accumulation of savings as well as meeting the minimum financial qualifications set down by the lending or insuring agency. Another factor, which impedes the supply of older low-cost housing, is the shortage of housing available for persons in the higher-income bracket. Those families who can afford but cannot get higher-quality or better-located housing represent a backlog of repressed demand as opposed to the ineffective demand of low and moderate-income families. Thus the "filtering process" is slowed down to the point that many low and moderate-income families live in substandard or crowded housing. Low and moderate-income families require substantial financial aid if they are to compete in today's housing market. An alternative is to supply homes in the price range which these families can afford. Thus far attempts at alleviating housing problems have been sporadic and piecemeal.

The major economic impediments to decent low-cost housing for low and moderate-income families are the lack of adequate income (as defined by the financial and insuring agencies) and the inability to meet required down payments. Increasing the general level of real income is a major task of the Federal government, although local officials should examine possible alternatives to increase the effective income of low and moderate-income families. Self Help and War on Poverty Programs are examples of programs designed to provide the participant with skills for use in the labor market.

The loan practices of financial institutions reflect current market situations as well as historical inertia. This is manifest in the down payment requirement even on government-insured loans. Down payments are viewed as a hedge against default by the borrower, the rationale being the larger the equity that a borrower has in property, the less likely he is to default on his loan. Under current housing market conditions, most mortgage loan officers making conventional loans consider a 20 to 30 percent down payment adequate protection against losses resulting from foreclosure.

Regulations of the Federal Home Loan Bank Board require that real estate loans not insured by the FHA or guaranteed by the VA be limited to 75 percent of the appraised value of the property. In some cases, savings and loan institutions may loan up to 90 percent of the appraised value up to a maximum appraised value of \$20,000. The maximum maturity period for all conventional loans made by Federal savings and loan associations is 25 years; however, the maturity period may be reduced at the discretion of the loan officer. Current practice of lending institutions making conventional loans is to issue mortgages at 75 percent of appraised value with a maturity period of 20 years. FHA loans are currently being made at 90 percent of appraised value with a 30 year maturity.

Although there are no hard and fast rules governing the financial capability ratios in determining the amount of loan to be granted, the rule of thumb of twice annual income has prevailed in most decisions. This ratio varies with the relative degree of tightness within the residential mortgage market and among different income levels. For example, FHA data for 1968 indicates that the value to income ratio of households who purchased new homes under section 203 generally increased as the household income increased. In 1968 the average value to income ratio was 1.84 for an FHA-insured new home. This figure was based on a sales price of \$25,227 and a total effective income* of \$13,877. Many factors are considered when a loan is granted, including down payment capability, earning potential, age, assets and liabilities, and income. The most important of these is the actual income stream allowed in computing the families' repayment capability. Usually the head of the household has his full income source counted, while the spouse or relative living within the same dwelling has some fraction of his total income counted as applicable toward the financial capability ratio. For lower-income families, a full consideration of the second source of income often means the difference between having the loan application accepted or rejected.

The following section presents data on initial occupancy costs for single-family dwelling units financed through conventional methods and FHA-insured. Data is also presented on rental apartment units having two and three bedrooms

*The FHA-estimated amount of the mortgagor's earning capacity (before deduction for Federal income taxes) that is likely to prevail during approximately the first third of the mortgage term.

INITIAL OCCUPANCY COSTS: CONVENTIONAL LOAN

The table below presents the major components of initial occupancy costs for a conventionally financed loan on a house costing \$20,000. The \$20,000 price was selected because it represents the lower limit which houses are currently being offered for sale and the upper limit which low and moderate-income households can afford. The figures are representative of values obtained from interviews with members of the financial community.

BASIC DATA

Appraised value	\$20,000
Loan/value ratio	75%
Principal	\$15,000
Interest rate	8½%
Loan fee	1% of principal
Mortgage maturity period	20 years

COST BREAKDOWN

Down payment	\$ 5,000
Loan fee	150
Fire insurance	40
Transfer fee	22
Recording fee	2
Tax (real estate, half year)	<u>257*</u>
	\$ 5,471

TOTAL COST

*Taxes are paid bi-annually in Santa Clara County. This figure represents one-half of the annual tax computed on the 1968 County average of \$10.30/\$100. If the house was built after March 1, the tax for the following fiscal year would be computed on the assessed value of the land only and would be considerably lower.

In Santa Clara County title search and insurance fees are traditionally paid by the seller. However, these costs are included as they are passed on to the buyer in the form of a higher selling price.

INITIAL OCCUPANCY COSTS: FHA-INSURED LOAN

The primary attraction of this type of Federally-insured mortgage lies in the possible reduction in financing costs. The following data was derived from interviews with members of the savings and loan industry, mortgage companies, and the quarterly publications of the FHA.

BASIC DATA

Appraised value	\$20,000
Loan/value ratio	90%
Mortgage amount	\$18,000
Interest rate	7 $\frac{1}{2}$ %
Mortgage maturity period	20 years
Loan fee	1% of principal

COST BREAKDOWN

Down payment: required minimum	\$ 1,000
actual payment	\$ 2,000
Loan fee	180
Fire insurance	40
Title transfer fee	22
Mortgage insurance	8
Recorder's fee	<u>2</u>
TOTAL COSTS	\$2,252

Loans currently issued under FHA-insured programs are going to the prime borrowers. The primary difference between FHA-insured loans and the conventional loan lies in the insurance feature which protects the lender against loss of principal, thus allowing more favorable terms with regard to down payment requirements and mortgage maturity period.

INITIAL OCCUPANCY COSTS: RENTAL APARTMENT

The following information is based on interviews with the Tri-County Apartment Association, Inc., and data from the 1969 Apartment House Vacancy Survey conducted jointly by the Santa Clara County Planning Department and San Jose State College. It should be stated at the outset that there is no set policy among apartment owners as to deposits for cleaning or rent security. This permits a great deal of discretionary power to be exercised by apartment owners in screening tenants.

Two cost ranges will be presented for the rental apartment model. The first is a two-bedroom, unfurnished apartment and the other is a three-bedroom unfurnished apartment. The assumption is made that the owner pays for the water and garbage. First and last month's rent are also assumed as required costs. The cleaning deposit is computed at 25% of the monthly rent.

BASIC DATA: Two-bedroom, unfurnished apartment.

COST BREAKDOWN

Median monthly rent	\$160
deposit	160
Cleaning deposit	<u>40</u>
TOTAL COSTS	\$360

BASIC DATA: Three-bedroom, unfurnished apartment.

COST BREAKDOWN

Median monthly rent	\$180
deposit	180
Cleaning deposit	<u>45</u>
TOTAL COSTS	\$405

The President's Committee on Urban Housing (Kaiser Report) has estimated the percent distribution which rental fees are allocated. The figures below are national averages and should be adjusted to reflect local conditions.

Payroll, management, and administration expense . . .	11%
Utilities	9%
Decoration, maintenance, and repair	6%
Taxes	14%
Insurance	2%
Debt retirement	42%
Vacancies and bad debt	9%
Profit and reserve	7%
TOTAL RENT ALLOCATION	100%

INCIDENTAL COSTS

Listed below is a table of other costs which are normally incurred during the initial phase of occupancy in a dwelling unit. While some costs, such as water and garbage, are borne by the owner of rental units, they are paid by the owner of a single-family dwelling. The fees or deposits listed below are paid by persons who have not been established in the area for a specified time, or in the words of one of the agencies contacted, "don't answer the right questions."

		Apartment	House
Garbage:	1. deposits	----	\$ 3.50
	2. monthly fee	----	1.75
Gas and Electricity:	1. apartment deposit	20.00	30.00
Telephone:	1. deposit fee	25.00	25.00
	2. installation fee	10.00	10.00
	3. minimum monthly fee	2.48	2.48
Water:		<u>no deposit</u>	<u>no deposit</u>
TOTAL		\$57.48	\$72.73

CHAPTER II MONTHLY OCCUPANCY COSTS

INTRODUCTION

The cost of occupying housing, whether borne by the private owner or a public agency, is a function of four key variables. They are 1) debt retirement; 2) taxes; 3) utilities; and 4) insurance. The aggregate sum of these variables constitute the majority of total monthly occupancy costs. They are usually paid on a monthly basis and are recurring as opposed to initial occupancy costs which are one-shot in nature. This study concentrates primarily on those costs directly attributable to the operation of the dwelling unit.

It is evident that monthly occupancy costs vary with the price of the dwelling unit. There are significant variations in the range of prices for homes. The following information is representative of average monthly occupancy costs. The data was derived from published information and interviews with members of the various agencies concerned.

MONTHLY OCCUPANCY COSTS: FHA-INSURED

The following assumptions are made for the FHA-insured model: \$25,000 value, mortgage amount \$23,000, $7\frac{1}{2}$ percent interest plus $\frac{1}{2}$ of 1 percent insurance fee, and 30 years maturity.

Payment to principal and interest	\$150.63
Mortgage insurance premium and others	<u>10.11</u>
Debt service	160.74
Hazard insurance	2.80
Taxes (real estate)	<u>46.28</u>
Total mortgage payment	209.82
Maintenance and repair	13.10
Heating and utilities	<u>23.60</u>
TOTAL COSTS	\$246.52

MONTHLY OCCUPANCY COSTS: CONVENTIONAL LOAN*

The following assumptions are made to develop the conventionally financed loan model: \$25,000 appraised value, mortgage amount \$20,000, 8½% interest rate, and a 20 year maturity period.

Debt service	\$173.57
Hazard insurance	2.80
Taxes (real estate)	<u>46.28</u>
Total mortgage payment	222.65
Maintenance and repair	13.10
Heating and utilities	<u>23.60</u>
TOTAL COSTS	\$259.35

Although the exact income requirement varies with the financial assets, liabilities and income stream of the borrower, the average income of those currently being granted a real estate loan for home purchase is approximately \$1,000 a month.

MONTHLY OCCUPANCY COSTS: RENTAL APARTMENT*

For those who cannot afford a new or used home, or do not wish to live in one, the most popular form of accommodation is the rental apartment. A survey conducted in March of 1969 revealed that the median rent for a three-bedroom unfurnished apartment was \$180 and a two-bedroom unfurnished apartment rented for a median price of \$160 a month.

	<u>Two-bedroom</u>	<u>Three-bedroom</u>
Rent	\$160	\$180
Utilities	<u>18</u>	<u>22</u>
TOTAL	\$178	\$202

*See Appendix II for a breakdown on the amount of subsidy involved under Section 235 and 236.

CHAPTER III
PROGRAMS AND POLICIES TO REDUCE OCCUPANCY COSTS

Santa Clara County has a number of organizations and agencies concerned with housing. A directory of such organizations has over a hundred entries.* The range of interests include, but are not limited to, fair housing, financing or non-profit sponsorship, professional and technical assistance and support, legal assistance, provision of housing information, and supporting legislative action. No successful attempt has been made to channel and focus these varied interests into a concerted plan of action for housing.

The Santa Clara County and San Jose Housing Authorities provide low cost housing for families of low and moderate income under the Section 23 Leased Housing Program. The program operates by having local housing authorities lease dwellings from private owners and make them available to low and moderate income families at rents they can afford. The two local authorities lease approximately 2,000 units for occupancy by low and moderate income families.

The Joint Cities-County Housing Element Program is a good example of local cooperation in focusing on the housing problem. Recognizing the need for an areawide approach to housing, the cities and the Planning Policy Committee of Santa Clara County have agreed to participate in a joint effort in identifying housing needs throughout the County. Information obtained from this study is to be used to coordinate the efforts of individual cities throughout the County, provide builders with data on expected housing needs, and document the progress of the housing program in the County.

*"Directory of Organizations and Agencies Concerned with Housing in Santa Clara County," Santa Clara County Planning Department, San Jose, California, June, 1969.

Private agencies have had limited success in providing housing for families of low and moderate income. Non-profit and limited profit sponsors have been hampered by a lack of funds, rising land and construction costs, and an unresponsive insuring agency at the federal level. Another problem related to non-profit sponsorship is the lack of expertise in handling the bureaucratic red tape usually associated with federal programs.

PROGRAMS NOT LOCALLY IMPLEMENTED

Other states and communities have taken an active role in the provision of low cost housing for their citizens. They have fully utilized the existing federal programs and passed enabling legislation to encourage innovative programs at the county and city level. Some of the programs do not involve a direct cash outlay on the part of the participating entity. For instance, the State of Connecticut offers tax abatement on some 221 (D) (3) housing units to the City of New Haven. Under this program, the tax abatement enables the sponsor to reduce rents for families who cannot afford the full rent. Other programs do involve a commitment of funds, but the money is leveraged so that some multiple of the original amount spent will be drawn out of the private sector. The following are other examples of programs communities have utilized in an attempt to solve their low-income housing needs.

LOAN GUARANTEES

Low-income housing efforts are often thwarted by the lack of funds which lenders are willing to put into decaying areas. In New York, a non-profit corporation guarantees loans for the use of private monies to back low-income housing efforts. The guarantee is a needed inducement to channel money into areas that would otherwise be an unacceptable risk for the financial community.

DOWN PAYMENT LOANS

Down payment requirements are one of the largest obstacles to home ownership. In New Haven, Connecticut, a local foundation will lend low-income families, without interest, the down payment required in 221 (D) (3) cooperatives. It will also guarantee the payment of carrying charges for families who can afford them but who do not satisfy FHA's rigorous mortgage credit requirements. This program enables families who are able to meet monthly costs, but not the down payment, to undertake home ownership without undue financial hardship.

PUBLIC HOUSING

Low-rent public housing can be made available to low income families through financial assistance provided by HUD to local housing authorities. Rents are established by the local housing authority and approved by HUD taking into consideration factors affecting rent-paying ability of families and financial stability and solvency of projects. Maximum rents cannot exceed 25 percent of family income. This program reaches deeper than interest subsidy programs in that federal assistance covers debt service on local authority bonds sold to pay for the development or acquisition of public housing.

SUPPLEMENTAL LOAN GUARANTEE

The City of Fresno has created an insurance fund to encourage private lenders to advance larger loans than they normally could consider in blighted areas. Should a home purchaser require a total mortgage of \$10,000 and the lender feels he can only advance \$7,000, the Housing Finance Board could issue a commitment to insure an additional \$3,000 to encourage the lender to make the full loan. The borrower is charged a fee of one-half of one percent of the total loan amount to meet the operating cost involved.

To protect its insurance commitments, the city is encouraging the various city departments to upgrade utilities and street maintenance in target areas.

DEMONSTRATION PROJECTS

Several cities have taken advantage of a special FHA-sponsored program to reduce housing costs. In Seattle, Washington, the CHOICE (Cost-Effective Home Ownership and Improved Contemporary Environment) pilot project was an attempt to join leaders of industry, the professions, labor, public-service institutions and governmental organizations in a concerted effort to show how best to produce lower cost housing with today's programs and technology. The results of this project was 2,500 net additions to the housing stock. Primarily aimed at moderate income families, the project enabled former apartment house dwellers to become homeowners.

Low income housing can be built if private citizens and public agencies are committed to providing decent housing for those in the lower income group. The programs described above are examples of what is being done elsewhere in an attempt to alleviate some of the burdens of the high cost of housing. In the next section, proposals to reduce the cost of occupancy housing and to increase the supply of funds for low cost housing projects are offered. The focus is primarily on financial aspects of housing families of low and moderate income.

CHAPTER IV RECOMMENDATIONS AND PROPOSALS

Housing is both a product and a process. As a product, it furnishes man with shelter, provides a setting for his daily activities, and in a larger sense, forms the nucleus of what has come to be known as a community. As a process, housing is a chain of events which encompasses the efforts of a fragmented and highly atomized residential construction industry, specialized financial institutions, a program of mortgage subsidies and insurance, and the filtering down of houses as people move to new residences. More than shelter, more than just a job, housing includes all of the immediate physical environment in which families and households live, grow, and decline. Decent housing for all should receive one of the highest priorities in our national goals.

On the contrary, however, housing has been relegated to a low position in terms of national priorities. Federal programs directed at low and moderate income families have been grossly underfunded and have experienced substantial difficulties in application. The State of California has appeared reluctant to establish or pursue significant housing programs, and local government has focused on accommodating a developer-dictated market. The mechanism of "filtering" has failed to provide an adequate supply of housing not only for low income families but also for those of moderate income.

These failures are even more apparent when contrasted to the achievements in providing housing for middle and upper income families. The quality and quantity of housing available for the effective part of the housing market provides a basis to extend efforts toward the substantial needs of those priced out of the present market.

The following proposals are offered as possible ways in which the volume and availability of low and moderately priced housing may be increased. There are basically two types of proposals offered: those which increase the availability of funds for mortgages, and those which lower the monthly and initial costs to occupy. They are neither mutually exclusive nor complimentary. It must be recognized that the market system responds quickest to the profit motive or when the possibility for profit is threatened. Thus, a program to increase the flow of funds into the mortgage market probably means greater returns to the investor and higher prices to the buyer. However, this is not always the case, for investors can be induced to place more funds into this market by offering tax incentives or threatening the loss of a tax free status. In this instance, the buyer would benefit from the increased availability of funds. Likewise, programs intended to reduce the cost to occupy decent housing work on some sort of tradeoff. Direct government subsidies reduce the cost to occupy in a real sense in that the family has more to spend on other goods and services. However, there are income restraints placed on the recipients. A program which lengthens the amortization period may keep monthly housing costs down but in the long run, total payments are higher.

There are no easy solutions to providing decent housing for all. Alternative strategies have been and will be constrained by institutional inertia. As long as housing is made a tool of monetary policy, as long as property rights are valued over human rights, the national housing goal of a decent home in a suitable living environment for all Americans will not be realized.

I. REDUCING THE COST TO OCCUPY HOUSING

A. Ownership

1. Property Tax Abatement:

Property taxes have an especially onerous impact upon low-income families. The problems of the poor and elderly are often cited in support of relative sweeping exemptions. However, implementation of such exemptions would involve problems of revenue replacement, with varying impact for various areas and individual local governments. A more moderate approach is to grant partial exemptions, with the local revenue loss made up by state grants.

For low-income elderly households, a property tax relief system should be enacted which entitles any such households to direct state reimbursement for the portion of its residential property tax that exceeds a specified percentage of the family income. To the degree that landlords can pass on property taxes in the form of higher rents, households that rent should have 25 percent of annual rent treated as property tax. The reimbursement schedule should be graduated inversely with income, so that those in the lowest income group receive the greatest relief with benefits gradually diminishing as income increases.

Another type of relief for poor elderly home owners who wish to avoid current property tax payment is to have the state pay the tax bill. This would create a lien on the property which would become due, with interest, upon the death of the owner or sale of the property.

2. Reducing Down Payments:

Down payment requirements are one of the greatest obstacles to home ownership by low and moderate income households. Although the amount of cash necessary to pay for the down payment varies with the amount of the loan and the selling price of the house, this direct outlay represents a substantial burden on low income household budgets. A buyer can take out a second mortgage on conventional financing but this only reduces his initial cash requirement and increases his monthly payments. FHA has a ban on second mortgages for its insured homes.

In order to increase the possibility for home ownership among low and moderate income families, the state should initiate a program of loans which would minimize down payments without raising monthly payments. A state fund created by state appropriations would be used to make loans to low and moderate income households to cover the initial costs to occupy a home. The loan would not begin to be repaid until the first mortgage is paid off or refinanced and would be a junior lien on the first mortgage. Interest could be charged from the day repayment began or, if this is not possible because of the FHA ban on secondary financing the loan should be interest free.

3. Lease and Sale of VA and FHA Foreclosed Dwellings:

Each year there are a number of VA and FHA foreclosures. Some of these units should be made available to low and moderate income families either through purchase or lease. Under a new proposal, by the administration, rents paid by public housing tenants would be applied as payment toward eventual ownership. The Housing Authorities could lease these units and make them available to families whose incomes are about to reach the maximum allowable limits. A portion of the monthly rent would count as

payment toward ownership, thus reducing the initial costs to occupy. When sufficient equity has been built up, the family could assume full responsibility for mortgage payments.

The attractive features of such a program are the increased possibility for home ownership by upwardly mobile families, the down payment requirement could be eliminated, racial and ethnic barriers to entry overcome, and units enter the market more quickly. The cost of administering such a program could be accommodated within the administration of the leased housing program.

4. Replacement Housing as a Cost of Public Improvements:

A valid criticism has often been levied that urban renewal and highway building have removed more low-cost housing units than they have replaced. Urban renewal programs have replaced low-income housing with high-cost housing and the highway projects have provided nominal relocation assistance. Only recently has the Federal highway program acknowledged responsibility to replace housing units it has had to remove.

At the state level, the Ralph Act has provisions for the replacement of housing removed for state highway construction. The replacement housing can be from existing houses, rehabilitated homes or new replacement housing. An owner of housing removed because of highway construction may select either replacement housing or accept the relocation benefits of the Federal-aid Highway Act of 1968. The Ralph Act has application in areas where the market value of real property is economically depressed, as determined by the State Highway Commission. These provisions should be enlarged to include areas of housing shortages. More importantly, the levels of responsibilities provided for in the Ralph Act should be assured for all public improvements by federal, state, and local agencies.

Efforts should also be made to provide a sharing by public and private agents for such actions caused by private developers.

B. Rental

1. Certificates of Decent Housing:

Government should not support substandard housing. Yet it has been estimated that between \$750 and \$850 million in Federal funds is used annually to pay for substandard housing, largely by housing costs paid by welfare recipients. Locally, it is estimated that \$13.5 million was allocated in 1969 by AFDC recipients for shelter. While there are no precise estimates as to the number of substandard units occupied by welfare recipients, available data indicates that "less-than-sound rentals are principally found in units costing less than \$120 per month."^{*} Low income families and welfare recipients cannot afford high rents and occupy housing in this rent category. To insure that the County is not subsidizing substandard housing through its housing allotments to welfare recipients, a program of certification of standard quality housing should be initiated.

The program could be closely tied to a vigorous code enforcement program and would result in the issuance of a certificate of decent housing for those units found to be in standard condition. The receipt and display of a certificate of decent housing should be made mandatory for landlords who rent to welfare tenants. Welfare tenants should be relieved of the duty to pay rent when code violations exist. Once repairs are made, provisions should be made to prevent an excessive rise in rents. The landlord, however, should not be denied a fair return on his investment.

*"The Housing Situation: 1969," Joint Cities-County Housing Element Pro

2. Conditional Income Supplement:

Public housing and cash grants are two methods to house the poor in standard housing. While the former assures the tenant is in standard housing, its scope has been limited in Santa Clara County. Cash grants do not assure that the recipient will spend the extra income for standard housing, nor will it necessarily increase the supply of standard housing. An alternative is to provide the low income family with income supplements on the condition that the family use all or a portion of the supplemental income to obtain standard quality housing. The conditional income supplement places a greater reliance on the private sector to provide decent housing and places emphasis on the ongoing process of upgrading the housing stock.

The lower income families would benefit in that the housing they occupy will be of standard quality. Making the supplement contingent upon the occupancy of standard housing is consistent with the necessity to keep the existing stock in decent condition. Landlords will have an incentive to rehabilitate or maintain their units as they see a demand for higher quality housing. Recipients of the income supplement may be allowed to keep any portion of the additional income they do not spend for housing. This allows them to make a choice as to the level of housing they wish to consume and will maintain competition in the market for lower priced units as well as moderately priced units.

3. Landlord-Tenant Adjudication Committee:

Landlord-tenant law looks on a lease as a conveyance of an interest in property subject to certain conditions and not as a contract of mutual obligation between parties. Because of the scarcity of low income housing,

as well as a lack of information about their rights, low income families are frequently forced to agree to almost any condition imposed by the landlord. Landlord-tenant law needs to be rewritten so that the legitimate interests of both parties are protected. Landlord should be required to provide decent, safe housing which meets housing code standards and to maintain the building in such condition. Likewise, tenants would be required to reasonably maintain their rented units.

When disputes arise, there presently is no vehicle available to settle the issue other than the courts. However, many issues do not require court settlement and could be resolved if some agency existed to serve such a function. A landlord-tenant adjudication committee comprised of both landlords and tenants could serve such a purpose. Because it would not be a judicial body, the committee could not enforce its decisions. However, it could serve a useful function of resolving daily issues which arise because of a misunderstanding of landlord/tenant rights and obligations. Should both parties agree, the arbitration could become binding, thus imparting a quasi-judicial authority to the committee and increasing its effectiveness.

C. Rehabilitation

1. Accelerated Depreciation on Rehabilitated Property:

Much of the housing stock of tomorrow is here today. The ongoing process of upgrading the current stock is not only desirable, it is imperative if we are to attain the national goal of a decent home and a suitable living environment for all Americans. Rehabilitating the stock that has fallen into substandard condition is one method of maintaining and increasing the supply of decent housing. However,

rehabilitation is costly and old residential properties cannot be profitably rehabilitated where the resulting value limits its use to families of low income unless the investor can have access to accelerated depreciation.

The law should be amended to provide for accelerated depreciation of rehabilitated properties at the same rates as for new construction. This would allow investors to go into marginal areas where the need for rehabilitation is greatest. Accelerated depreciation on rehabilitated units would allow the owner to lower his rents, thus bringing the rent on his units within the reach of low and moderate income families.

2. Write-Down Subsidies:

Local renewal agencies can acquire a property for resale to a private owner subject to an obligation to rehabilitate. Because of the obligation to rehabilitate, the market value of the property is deflated. In most cases, the difference between the acquisition cost and sales prices is charged to the renewal agency budget as a project expenditure. The same principle can be applied to the owner of a substandard housing unit in a renewal area. The agency could provide a "write-down" subsidy to the present owner of a substandard housing unit with the stipulation that he rehabilitate the unit.

This program could be coupled with a vigorous housing code enforcement program and extended outside urban renewal areas. Heretofore, building inspectors looked the other way when they saw code violations, as a vigorous enforcement program would have caused hardships upon most of the occupants of substandard houses. However, if the write-down subsidy were provided to owners of substandard units who agreed to rehabilitate their units, code enforcement could serve as a catalyst in speeding the renewal and rehabilitation process.

II. INCREASING THE SUPPLY OF MORTGAGE FUNDS

A. State Below Market Loans:

The state should have a housing loan program to augment federal programs. The state could issue tax-exempt bonds to finance housing at below market rates. Legislation should authorize loans to nonprofit and specially defined limited profit corporations as well as to individuals. Such a program would allow the state as well as the federal government to influence the supply of low and moderate income housing. The program could also encourage more housing by permitting greater flexibility than under Federal programs. This could include such items as not requiring a community to have a workable program, allowing more than 6% return to limited profit developers, less complex administration, and innovations such as rent-skewing--in which the higher rents of some tenants support the lower rents of others--to achieve the same ends as rent supplement programs. A state program is needed to compensate for the ever-present deficiencies in federal funding of programs so that an adequate supply of low and moderate income housing could be made available both for ownership and rental.

B. Cost Limit Aid:

Federally aided housing programs have prescribed cost standards. Because construction and finance costs are higher in California than in most of the rest of the country, even the most efficiently planned projects may fail to fall within federal cost standards. To enable the developer's total mortgage to fall within federal cost limitations, the state could make interest-free loans for up to 10% of the development cost of the project. Such a loan would be paid off only after the federally aided mortgage is paid or refinanced. It would be a lien on the property but subordinate to the FHA first mortgage. (FHA has indicated approval of this type of estate assistance since it does not constitute currently prohibited second mortgage.

C. Use of Short-Term County Funds:

The County has a considerable sum of short-term funds. Some portion of this fund could be deposited in banks and savings and loan associations that agree to invest an equivalent amount for interim financing of federally insured housing projects for low and moderate income families. This would provide construction funds for developers in the interim period between the commitment of federal or guaranteed funding and the time when the permanent financing takes effect.

D. State Mortgage Authority:

Financial institutions investing in mortgages are limited in the total amount of funds they can allocate for this purpose because of the long term nature of these loans. Funds are tied up for 20 to 30 years because there is no well-developed secondary market for conventionally financed mortgages. The creation of a State Mortgage Authority could free millions of dollars for home construction and mortgage loans.

The Authority could sell bonds to obtain capital that would be used to purchase existing mortgages from lending institutions. These institutions would be able to sell their older, lower-yield mortgages--those bearing 6.0 percent interest and below--to the Authority, thus freeing capital for future loans. The money freed from the sale of older mortgages could be tied so that a certain portion, say 25 percent, would have to go to low and moderate income housing and the remainder would have to be allocated to other homebuilding and purchase loans within the state. The money could be further tied in that the loans going to low and moderate income families would have to bear an interest rate at least 1 percent below market rates, and no points or discounts charged.

The State of New York has recently passed legislative approval for the creation of a \$750 million State Mortgage Authority. California should follow the example of New York to bolster the housing industry to alleviate our traditional reliance on out-of-state funds for mortgage financing.

The creation of a State Mortgage Authority would not only benefit the lending institutions, who would receive increased revenue from the fees they charge, but also the families of low and moderate income since 25 percent of all monies released from secondary market operations of the Authority would have to go into low and moderate income housing at below market rates.

E. Differential Reserve Requirements on Loans:

The availability of mortgages for low and moderate income families can be influenced through direct and indirect methods. Direct methods compel financial institutions to allocate a specified percent of their portfolios for low income housing. Indirect methods include moral suasion, tax incentives, and differential reserve requirements on loans. The latter method is particularly interesting because it is a departure from the usual reserve requirement mechanism. Presently, reserve requirements are placed on deposits but not on loans. Thus, there are no effective means of controlling the composition of bank portfolios.

Banks and savings and loan associations can be encouraged to invest more in low and moderate income housing if differential reserve requirements are placed on loans. Reserve requirements on loans for low income housing could be substantially lower than commercial loans if the desire is to increase the amount of loans for low cost housing. By changing reserve requirement on the type of loan granted instead of the type of deposit, Federal Reserve Board actions can influence the investing patterns of banks and savings and loan associations.

F. Direct Federal Lending:

Federal housing programs which reduce interest charges to as low as 1 percent for the consumer bear a market rate of interest to the government. At the maximum participatory rate, the Federal government's contribution for interest on a \$20,000 mortgage may exceed the value of the principal. Thus, it would be more economical to substitute direct federal lending for interest subsidies on market-rate mortgages.

In the long-run, the government can usually borrow money in the open market at a lower cost than the market rate of interest on residential mortgages. The main reason direct lending is not used is the budgetary constraint, which treats the purchase of mortgages as a direct budget expenditure even though they are income producing and self-liquidating. If the federal budgetary system were modified to include a capital budget system, direct federal lending could be used in place of interest subsidies with considerably less total cost to the government.

G. Federal Insurance for Conventional Mortgages:

The only mortgages which are insured for a substantial portion of the outstanding loan are those covered by FHA or VA. The combined total of these programs represent about one-third of the total outstanding mortgages on the market. Conventionally financed mortgages (those without an insurance or guarantee feature) far exceed the amount secured by FHA-insured or VA guaranteed programs. The salient feature of federally insured programs is the low or no down payment requirement. As previously noted, down payment requirements are the largest obstacle to occupancy of decent housing.

Federal insurance for conventional loans could bring the possibility of home ownership closer to many families who do not presently qualify for mortgages. The insurance feature could lower the down payments and extend the amortization period. Since the loan is guaranteed against loss of principal, the mortgages' liquidity and general investment attractiveness should be greatly enhanced. This serves a twofold purpose in that home ownership can be realized by more families and the funds available for mortgage loans would be increased.

The experience of FHA in its new home program (Section 203), indicates that the insurance program would not be a financial burden on the budget. In fact, FHA has accumulated a substantial reserve of funds from the fee it charges for the insurance protection. Legislation authorizing and funding a federal insurance program for conventional loans would be an appropriate area for congressional action.

H. Pension Fund Investment:

One relatively untapped source of home financing is the assets in various pension and retirement funds. On a national scale, these funds currently invest about 8 percent of their assets in mortgages. Several progressive groups in California, including the Public Employees Retirement System and the California Carpenters Pension Trust, have pledged considerable percentages of their available funds for home building. Substantial increases in the supply of funds for housing would be forthcoming if all pension and retirement funds were required to invest 25 percent of their available assets in mortgages. Fuller participation could be insured if those funds who elect not to invest 25 percent of their funds in mortgages were to lose their tax free status.

I. Mortgage Insurance for Rehabilitation:

Investors in residential mortgages seek the greatest return from their dollar commensurate with acceptable risks. Thus, it is consistent with this aim to shy away from areas where the potential risk of default is greater than the expected return. Yet it is in these very areas that the need for money exists. Rehabilitation and maintenance of the older housing stock is imperative to insure an adequate supply of decent housing. The 1969 Housing Act makes some provisions for insuring loans made in code enforcement, urban renewal, and in so-called grey areas. However, the funding is inadequate to meet the demands for such loans. Supplemental programs similar to federal programs should be developed at the local level.

Local government should set up special loan insurance funds to be used to insure loans made in older areas. The insurance feature may be the necessary inducement to encourage lenders to make mortgages or rehabilitation loans to residents in areas which have started to decay. The attractive feature of an insurance type of program is that money for this purpose has a multiplier effect, i.e., for every dollar used for insurance purposes, some multiple of this dollar is induced from the private sector. A nominal fee could be charged for this insurance privilege which would make the fund self-supporting.

J. Variable Interest Rates:

Most mortgages bear a fixed rate of interest. Given the long terms on which most mortgages are amortized, chances are good that the market rate of interest will vary during this period. This puts a burden on the holder of the mortgage bearing a lower interest rate because he can sell them only at a substantial discount. In periods of inflation and high interest rates, the

supply of funds available for mortgage loans shrinks because investors do not want to be saddled with long-term, low yield paper when there is an opportunity for higher returns with relatively quick turnover.

In order to increase the attractiveness of the mortgage, their yield must be comparable to other paper bearing similar risk factors. This can be done by having a variable interest rate. The rate of interest on the mortgage could be tied, by some formula, to some established market rate such as the rate on AAA corporate bonds. Monthly mortgage payments would not necessarily rise, but as the interest rate increases, a smaller portion of the payment would be allocated toward paying off the debt and more would go toward interest. In a similar manner, large amounts of the mortgage payment would go to the principal as interest rates decline. Depending on the yield on AAA corporate bonds, the length of time required to completely amortize the mortgage would be longer or shorter.

Since the yield on mortgages would be comparable to other forms of paper bearing similar risk, institutional investors would find mortgages an attractive investment. This would increase the flow of funds into the mortgage market and thereby increase the availability of money for mortgage loans. The variable interest rate plan has appeal for the purchaser since it is possible for him to benefit from monetary policy which lowers the interest rate. The variable interest rate scheme is more attractive than the escalator clauses found in some mortgages. Under certain escalator clause plans, interest rates can rise above but never drop below the initial contract rate.

K. Split Mortgages:

Most homes are purchased under the conventional system of land tenure in which the land is purchased with the house. Both land and improvements are amortized over the term of the mortgage. In effect, this forces the low income homeowner to save his money by building an equity--but low income households usually do not have incomes which would support savings. There is no inherent reason why land, which never disappears, should be paid off over the same period as the building shell which may be good for about 50 years.

One device to accomplish differential amortization is a "split mortgage." A split mortgage could amortize the building over 50 years, improvements such as heating and appliances over 10 years, and not amortize the land at all. This would, in effect, cause a leasehold on the land. A split mortgage could lessen monthly housing payments and enable more low and moderate income families to experience home ownership of units of higher quality than those possible under conventional mortgages. Opportunities could be incorporated to permit the owner of the improvements to purchase the fee title to the land should he desire to exercise this option.

L. Piece of the Action Mortgages:

Mortgage lenders need more inducement than the current rate of return on their loans if there is to be an increased flow of money into the mortgage market. Points or discounts have not been sufficient to significantly influence the flow of capital into this market when alternative sources of investment have offered a greater rate of return.

The "piece of the action" mortgage may induce investors back into the mortgage market. In one variation of this method, the lender gets a percentage of the rent or profits on rental or commercial property. In the single family residences, the lender could share in the appreciation of a property at the time of resale. This could help lower income family in that the availability of funds for home mortgages would be increased as investors see an opportunity for increased returns. As more new home loans are granted, the filtering process is speeded and more used housing becomes available for those unable to purchase new units. Monies for rehabilitation purposes would also be more readily available as investors would have a direct interest in keeping up the value of the property.

M. Industry Seed Money:

Santa Clara County is an attractive area in which to locate many types of industry. The transportation network and industrial infrastructure are well developed, and there is a trained labor force. These and other factors have generated large increases in economic expansion in the past two decades. Santa Clara County has experienced a rapid expansion of its industrial base, but insufficient attention has been given to the housing needs of the growing population, particularly for families of low and moderate income.

Just as people are attracted to areas of expanding employment opportunities, industrial firms are similarly attracted to areas where the existing infrastructure is well established and markets can be expanded. As firms benefit from locating in this area, they should contribute to solving some of the problems created by their presence. Local employers could be charged a fee to provide a revolving fund for housing low and moderate income families.

Such a fee could be levied on a proportionate basis with the number of lower paid positions weighted heavier than positions in management. The fee could be collected similarly to the business tax, thus reducing the cost of administering the program, and could be deducted as a legitimate operating expense by employers. The exact amount of the fee to be levied would, of course, depend on the anticipated increase in new firms and the desired amount of capital to be available in the revolving fund.

The revolving fund would be an incorporated body coming under the California Not-For-Profit Corporation Statute. The primary purpose of this fund is to provide low-rate, short term loans to limited-profit and nonprofit sponsors of housing for families of low and moderate income. Possible uses for short term loans would be to finance project development costs, to finance the acquisition of land, and to promote innovative educational and training programs.

With industry providing the seed money for low-income housing projects, local government could pursue its growth policy and still make some provision for housing the new employees attracted to the area because of increased employment opportunities.

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APPENDIX I

The following descriptions of major federal programs for low and moderate income housing that are in use or could be used in Santa Clara County are taken from "HUD Programs," a publication of the Department of Housing and Urban Development.

INTEREST SUPPLEMENTS ON HOME MORTGAGES

A program to enable low-income families to buy a home or a membership in a cooperative housing project.

Nature of Program

HUD makes monthly payments to the mortgagee to reduce interest costs to as low as 1 percent on a home mortgage insured by the Federal Housing Administration. The homeowner must pay at least 20 percent of his adjusted monthly income on the mortgage. Amounts of subsidies vary according to the income of the individual homeowner and the total amount of the mortgage payment at the market rate of interest. Family income and mortgage limits are established for eligibility in each locality. Assistance may be provided for new or substantially rehabilitated homes and, in a limited number of cases, for existing homes without rehabilitation.

Applicant Eligibility

The applicant may be anyone whose income qualified him for the subsidy aid.

Application is made to a lending institution approved by FHA as a mortgagee.

Information Source

Local FHA insuring office.

Legal Authority

Section 235, National Housing Act (Public Law 73-479), as added by the Housing and Urban Development Act of 1968 (Public Law 90-448).

Administering Office

Assistant Secretary for Mortgage Credit--FHA Commissioner, Office of Assistant Commissioner for Multifamily Housing.

INTEREST SUPPLEMENTS ON RENTAL AND COOPERATIVE HOUSING MORTGAGES

A program to reduce costs on certain rental and cooperative housing projects designed for occupancy by low-income families.

Nature of Program

HUD makes monthly payments to mortgagees, on behalf of mortgagors, of a part of the interest on market-rate mortgages financing rental or cooperative housing projects for low-income families. Interest-reduction payments may also be made on rental or cooperative housing projects owned by private nonprofit, limited-dividend, or cooperative entities which are financed under a State or local program providing assistance through loans, loan insurance, or tax abatement.

Interest-reduction payments cannot exceed the difference between the amount required for principal, interest, and mortgage insurance premium on a market rate mortgage and the amount required for principal and interest on a mortgage at 1 percent interest. The purpose of the payments is to bring the monthly rental charges down to a level that low-income families can afford to pay with at least 25 percent of their adjusted monthly income.

Applicant Eligibility

Applicants for mortgages insured by the Federal Housing Administration and for interest-reduction payments may be nonprofit, limited-dividend and cooperative entities.

Applications for insured mortgages are made to lending institutions approved by FHA as mortgagees.

Applications for interest-reduction payments where no FHA insurance is involved are made directly to the local FHA insuring office.

Information Source

Local FHA insuring office.

Legal Authority

Section 236, National Housing Act (Public Law 73-479), as added by the Housing and Urban Development Act of 1968 (Public Law 90-448).

Administering Office

Assistant Secretary for Mortgage Credit--FHA Commissioner, Office of Assistant Commissioner for Multifamily Housing.

LOW-RENT PUBLIC HOUSING

A program to help public agencies provide decent, safe, and sanitary housing for low-income families at rents they can afford.

Nature of Program

Financial and technical assistance is provided by HUD to local housing authorities to plan, build and/or acquire, own, and operate low-rent public housing projects. Federal annual contributions are made to cover the debt service on local authority bonds sold to pay for the development or acquisition of public housing. HUD financial assistance is also provided in the form of preliminary loans to the authority for planning, and temporary loans to build, low-rent housing, as well as the annual contributions subsidies.

The local housing authority provides housing in various ways--by construction, by rehabilitation of existing structures, by purchase from private developers or builders (the Turnkey method), and through lease from private owners--and then rents these dwellings to low-income families. Special provisions allow for the purchase of such housing by low-income families under a variety of homeownership programs.

There are special provisions for people of limited income which apply in the public housing program; in particular, there are special subsidies for those displaced by urban renewal or other governmental action or by natural disasters, for the elderly and the handicapped, and families of unusually low income or with more than four minors.

Applicant Eligibility

Applicants must be local housing authorities established by a local government in accordance with State law, authorized public agencies, or Indian tribal housing authorities. The proposed program must be approved by the local governing body. The community must have a certified Workable Program for Community Improvement.

Application is made to the HUD regional office serving the locality.

Information Source

Assistant Regional Administrator for Housing Assistance, HUD regional office; or Deputy Assistant Secretary for Housing Assistance, Housing Assistance Administration, Washington, D.C. 20413.

Legal Authority

U.S. Housing Act of 1937 (Public Law 75-412), as amended.

Administering Office

Assistant Secretary for Renewal and Housing Assistance, Housing Assistance Administration.

LOW-RENT PUBLIC HOUSING--LEASING

A program to provide low-rent public housing for low-income families through the use of private housing accommodations.

Nature of Program

Annual contributions made to authorized local public agencies enable them to work with real estate agencies, owners, and developers in providing housing for low-income families. Local housing authorities lease dwellings from private owners and make them available to low-income families at rents they can afford. Local authorities may also acquire structures containing leased units and sell these units to the tenants on terms that would enable them to make the purchase without undue financial hardship.

Applicant Eligibility

Applicants may be local housing authorities and other authorized public agencies. The local governing body must have passed a resolution approving the application of the housing program to the locality.

Application is made to the HUD regional office serving the locality.

Information Source

Assistant Regional Administrator for Housing Assistance, HUD regional office; or Deputy Assistant Secretary for Housing Assistance, Housing Assistance Administration, Washington, D.C. 20413.

Legal Authority

Sections 23 and 10(c), U.S. Housing Act of 1937 (Public Law 75-412), as added by the Housing and Urban Development Act of 1965 (Public Law 89-117) and amended by the Housing and Urban Development Act of 1968 (Public Law 90-448).

Administering Office

Assistant Secretary for Renewal and Housing Assistance, Housing Assistance Administration.

RENT SUPPLEMENTS

A program to make decent housing available to low-income individuals and families.

Nature of Program

Federal rent supplement payments are made to owners of certain private housing projects. The rent supplement payment for a tenant amounts to the difference between 25 percent of his income and the basic rental for the unit he occupies. As the tenant's income changes, the rent supplement is increased or decreased accordingly. If his income rises to the point where he can pay the full rent, he may continue living in the same unit without rent supplement.

The housing on which rent supplements are paid must be financed under certain HUD programs, or under State or local programs that provide loans, loan insurance, or tax abatements--if the projects are approved for rent supplement before completion of construction or rehabilitation.

Applicant Eligibility

Tenants whose incomes fall within prescribed limits may be eligible for rent supplements if they also qualify in one of the following ways: are elderly or handicapped (or have an elderly or handicapped wife or husband); are displaced by governmental action; are occupants of sub-standard housing; are present or former occupants of dwellings damaged or destroyed by a natural disaster since April 1, 1965.

Tenants apply to the owner of the housing project.

Housing owners eligible for contracts to receive rent supplements are nonprofit, cooperative or limited-dividend organizations. Owners apply for rent supplement contracts at HUD regional offices.

Information Source

Assistant Regional Administrator for Federal Housing Administration, HUD regional office; or local FHA insuring office.

Legal Authority

Title I, Housing and Urban Development Act of 1965 (Public Law 89-117) as amended.

Administering Office

Assistant Secretary for Mortgage Credit--FHA Commissioner, Office of Assistant Commissioner for Multifamily Housing.

APPENDIX II

HOMEOWNERSHIP ASSISTANCE FOR LOWER-INCOME FAMILIES SECTION 235 INTEREST SUBSIDY PROGRAM

The following example indicates the amount of interest subsidy a family of four could receive under Section 235 homeowner assistance. Two formulas are used to determine the interest subsidy, the HUD contribution being the lesser of the two.

BASIC INFORMATION

INCOME

Total Annual Income	\$ 7,300.00
Adjusted Annual Family Income	6,335.00

AREA INCOME LIMITS FOR THIS FAMILY	7,090.00
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HOME INSURANCE TRANSACTION

Sales Price	17,700.00
Mortgage Amount	17,500.00
Downpayment	200.00
Terms in Months	360.00
Interest Rate	7 $\frac{1}{2}$ %
Mortgage Insurance Premium (MIP)	1%

TOTAL MONTHLY MORTGAGE PAYMENT

Debt Service	128.45
Hazard Insurance and Real Estate Taxes	46.31
Total Monthly Mortgage Payment	<u>174.76</u>

ASSISTANCE CALCULATIONS

FORMULA I

Total Monthly Mortgage Payment	174.76
20% of Adjusted Monthly Income	<u>105.58</u>
Formula I Subsidy	69.18

FORMULA II

Monthly Payment (Principal + Interest + MIP)	128.45
Monthly Payment (Principal + Interest @ 1%)	<u>56.35</u>
Formula II Subsidy	72.10

The HUD interest subsidy would be the lesser of the two amounts determined by Formula I and II or, \$69.18. The breakdown of total monthly mortgage payment is given below.

Family's monthly mortgage payment	105.58
HUD interest subsidy	<u>69.18</u>
Total Monthly Mortgage Payment	174.76

RENTAL HOUSING FOR LOWER-INCOME FAMILIES
SECTION 236 INTEREST SUBSIDY

The following example is illustrative of the amount of rent reduction a family of four could receive under Section 236 rental housing. A renter under the 236 program pays 25 percent of his adjusted income or the basic rent, whichever is greater. Income requirements are the same as for Section 235. The basic rent is computed on the basis of a mortgage bearing an interest rate of 1 percent rather than the full market rate.

BASIC INFORMATION

INCOME

Total Annual Income	\$7,300
Adjusted Annual Family Income	6,335

AREA INCOME LIMITS FOR THIS FAMILY	7,090
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RENTS

Market Rent	165
Basic Rent	110

ASSISTANCE CALCULATION

25% of Adjusted Monthly Income	132
Basic Rent	110

The family would pay the greater of the two rents computed in the Assistance Calculation section or \$132. The HUD contribution in the form of interest subsidy is \$165 - \$132 or \$33.

RENT SUPPLEMENT PROGRAM

Families and individuals who are eligible for rent supplement pay 25 percent of their gross annual income for rent. The difference between this amount and the basic rent for a unit represents the amount of rent supplement for that family or individual.

The following example illustrates the amount of rent subsidy a family of four would receive under this program.

INCOME

Total Annual Income	\$3,600
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RENT

Market Rent	165
Basic Rent	110

ASSISTANCE CALCULATION

Basic Rent	110
25% of Monthly Income	<u>75</u>
Total Monthly Rent Subsidy	35

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